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RESEARCH SYMPOSIUM
THURSDAY SESSIONS

**Incentive Contracts: The Attributes that Matter Most in Driving
Favorable Outcomes**

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by

Robert L. Tremaine, Defense Acquisition University

**4th Annual Acquisition Research Symposium
of the Naval Postgraduate School:**

**Acquisition Research:
Creating Synergy for Informed Change**

May 16-17, 2007

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ACQUISITION RESEARCH PROGRAM
GRADUATE SCHOOL OF BUSINESS & PUBLIC POLICY
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Attn: James B. Greene, RADM, USN, (Ret)
Acquisition Chair
Graduate School of Business and Public Policy
Naval Postgraduate School
555 Dyer Road, Room 332
Monterey, CA 93943-5103
Tel: (831) 656-2092
Fax: (831) 656-2253
E-mail: jbgreene@nps.edu

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Proceedings of the Annual Acquisition Research Program

The following article is taken as an excerpt from the proceedings of the annual Acquisition Research Program. This annual event showcases the research projects funded through the Acquisition Research Program at the Graduate School of Business and Public Policy at the Naval Postgraduate School. Featuring keynote speakers, plenary panels, multiple panel sessions, a student research poster show and social events, the Annual Acquisition Research Symposium offers a candid environment where high-ranking Department of Defense (DoD) officials, industry officials, accomplished faculty and military students are encouraged to collaborate on finding applicable solutions to the challenges facing acquisition policies and processes within the DoD today. By jointly and publicly questioning the norms of industry and academia, the resulting research benefits from myriad perspectives and collaborations which can identify better solutions and practices in acquisition, contract, financial, logistics and program management.

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Incentive Contracts: The Attributes that Matter Most in Driving Favorable Outcomes

Presenter: **Robert L. Tremaine**, is an Associate Dean for Outreach and Performance Support at the Defense Acquisition University's West Region campus in San Diego, CA. He is an Air Force Academy graduate and holds a Master's of Science in Systems Management (Research and Development) from the Air Force Institute of Technology. He is a retired Air Force colonel with over 25 years' experience in air, missile, and space weapon systems acquisition.

Abstract

Incentive contracts have been in place for many years. They represent just one of many contractual tools the Department of Defense has at its disposal to drive certain performance behaviors. Lately, the usefulness of incentive contracts has come into question. The dividends have not been readily apparent. This research study set out to determine what generally afforded strong correlations between incentive-type contracts and expected performance outcomes. Twenty-five weapon system acquisition programs offices were interviewed in various stages of their acquisition lifecycles. A standardized questionnaire-survey was used to capture the data. This presentation prepared for the Fourth Annual Acquisition Research Symposium will address the findings and include a few key recommendations intended to better arm the acquisition workforce on the use of incentive contracts.

Discussion

In the past several years, major weapon system development programs have drawn significant attention. The reasons are varied. In some cases, costs have skyrocketed; schedules have experienced significant delays; and performance levels have failed to meet government expectations despite the employment of management tools designed to control costs, preserve schedules and influence performance outcomes. Some of these management tools (including contractual measures, as originally conceived and specified by the *Federal Acquisition Regulations (FARs)*) can give tremendous flexibility to the implementation of government contracts. The use of such contractual measures is one of many handy tools in a program manager's toolkit to help drive performance behavior. However, the GAO recently identified an apparent disconnect between the use of certain measures like incentives and expected outcomes in weapon system acquisitions. In short, it appeared that incentives were not driving performance outcomes as originally envisioned.

So, what about incentives? Are they still a good tool to drive performance behaviors despite the recent criticism and doubt? Have organizations found a way to effectively apply incentives and demonstrate the usefulness of incentives? The answer to all of these questions is, "yes." There is no "one size fits all," but the incentive attributes that seemed to matter the most in influencing performance outcomes for the 25 programs, and generally afforded strong correlations between incentives and desired performance were indicated by the findings.



Conclusion

Strongly Communicated Expectations and Feedback: Frequent and unambiguous communication/feedback made a noticeable difference for incentive contracts. Even though incentive contracts require some additional administrative burden, the outcome justified the increased workload of feedback for most programs under this research review. Continuous and open dialogue at both junior and senior levels led to early discovery and timely reconciliation of many known issues and helped keep a program on track.

Metrics: The selection of key and enduring measures within an evaluation period and of measures that could be connected to subsequent evaluation periods made a noticeable difference for incentive contracts. Key measures can validate whether or not a program achieved certain necessary intermediate milestones along a program's critical glide path. They confirm program momentum. They served as an early warning system—a bell weather—and answer the age old question, "Are we on track"? They also fill a huge role as performance benchmarks. Those interviewed under this research project said when they effectively employed key measures, such tools also helped them navigate their program pathway despite the unavoidable programmatic turbulence. Their measures surfaced either as two types: objective and/or subjective. Without question, selecting the correct type of measures presented the biggest challenge. The ability to hard-wire them to achievable outcomes makes objective measures like Technical Performance Measures (TPMs), Cost Performance Indices (CPIs), Schedule Performance Indices (SPIs), etc., invaluable gauges. They served as tremendous forecasting devices when they were carefully connected to outcomes.

Base Fee: The incorporation of base fee in award-fee contracts made a noticeable difference. Of the 25 organizational interviews, many used some form of base fee on cost-plus-award-fee contracts. Numerous organizations implementing cost-plus-award-fee (CPAF) valued base fees as a leverage tool. Even though the *Federal Acquisition Supplement (DFARS) 216.405-2(c)(iii)* allows up to 3% of the estimated cost of the contract exclusive of fee, a contractor could provide "best efforts" for the award-fee term and still receive no award. As a result, there was some pressure on the government to provide a portion of the award fee for "best efforts." Further, our research team found that senior defense industry personnel welcomed the use of base fee to better delineate the difference between "best efforts" (e.g., fee) and "excellence" (e.g., award).

Trained and Experienced Personnel: Training and experience made a noticeable difference for incentive contracts. Nothing seems to have a more dramatic impact in DoD like training and experience. Training draws its roots from practical experience. It's systematic. We learn from our successes and failures in the field and make adjustments accordingly in the way we train. The mantra, "we train like we fight and fight like we train" is pervasive within the warfighter arena and, ultimately, leads to advantages on the battlefield. Without question, practical experience helps build better training programs. It can overcome unforeseen shortfalls and the inevitable prevailing uncertainty even within proven systems. It's no different for incentive-type contracts. Organizations that had formalized instruction and/or coached their personnel on the use of incentives indicated such training more favorably influenced outcomes.

The exploitation of an increasingly popular collaborative medium called Communities of Practices (CoPs) on the DAU Acquisition Community Connection offers access to these particular techniques and an even wider array of current experiences and lessons learned regarding incentives ranging from the general to the specific. The DAU has already established a site on the ACC, Award and Incentive Fee Contracts. See



(<https://acc.dau.mil/CommunityBrowser.aspx?id=105550>). These and other collaborative training aids are critical because once an incentive strategy is in place, its maximum value truly depends on its ability to implement techniques that drive favorable outcomes. There's no better source of experts who face contract incentive challenges every day than the acquisition workforce who is charged with appropriately implementing the techniques that drive outcomes, appreciably.



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2003 - 2006 Sponsored Acquisition Research Topics

Acquisition Management

- Software Requirements for OA
- Managing Services Supply Chain
- Acquiring Combat Capability via Public-Private Partnerships (PPPs)
- Knowledge Value Added (KVA) + Real Options (RO) Applied to Shipyard Planning Processes
- Portfolio Optimization via KVA + RO
- MOSA Contracting Implications
- Strategy for Defense Acquisition Research
- Spiral Development
- BCA: Contractor vs. Organic Growth

Contract Management

- USAF IT Commodity Council
- Contractors in 21st Century Combat Zone
- Joint Contingency Contracting
- Navy Contract Writing Guide
- Commodity Sourcing Strategies
- Past Performance in Source Selection
- USMC Contingency Contracting
- Transforming DoD Contract Closeout
- Model for Optimizing Contingency Contracting Planning and Execution

Financial Management

- PPPs and Government Financing
- Energy Saving Contracts/DoD Mobile Assets
- Capital Budgeting for DoD
- Financing DoD Budget via PPPs
- ROI of Information Warfare Systems
- Acquisitions via leasing: MPS case
- Special Termination Liability in MDAPs

Logistics Management

- R-TOC Aegis Microwave Power Tubes
- Privatization-NOSL/NAWCI
- Army LOG MOD



- PBL (4)
- Contractors Supporting Military Operations
- RFID (4)
- Strategic Sourcing
- ASDS Product Support Analysis
- Analysis of LAV Depot Maintenance
- Diffusion/Variability on Vendor Performance Evaluation
- Optimizing CIWS Lifecycle Support (LCS)

Program Management

- Building Collaborative Capacity
- Knowledge, Responsibilities and Decision Rights in MDAPs
- KVA Applied to Aegis and SSDS
- Business Process Reengineering (BPR) for LCS Mission Module Acquisition
- Terminating Your Own Program
- Collaborative IT Tools Leveraging Competence

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Award and Incentive Fee Contracts

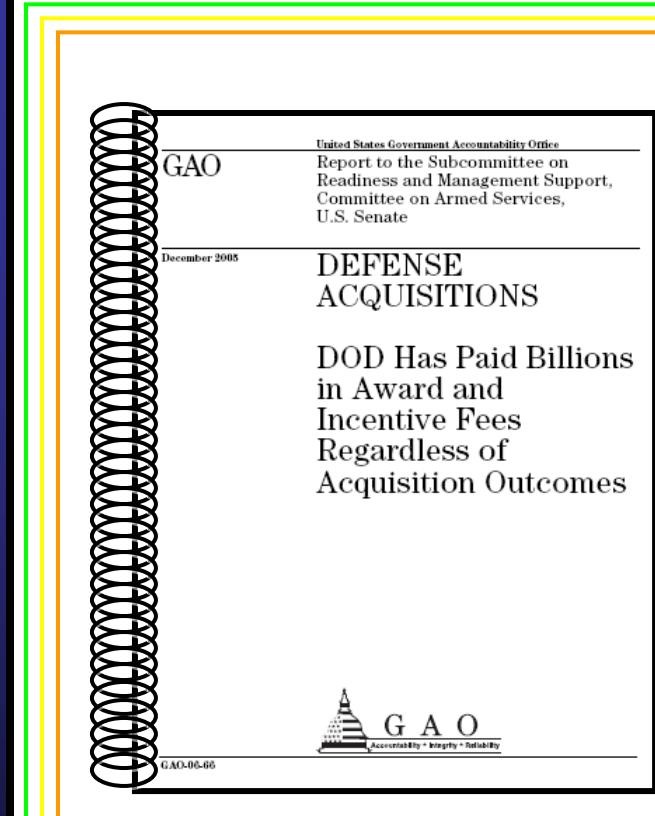
GAO's Findings

Background

Study Proposal

Study Findings

Recommendations



Why GAO Did This Study

GAO was asked to determine whether award and incentive fees have been used effectively as a tool for achieving DOD's desired acquisition outcomes. To do this, GAO selected a probability sample of 93 contracts from the study population of 597 DOD award- and incentive-fee contracts that were active and had at least one contract action valued at \$10 million or more from fiscal year 1999 through 2003.



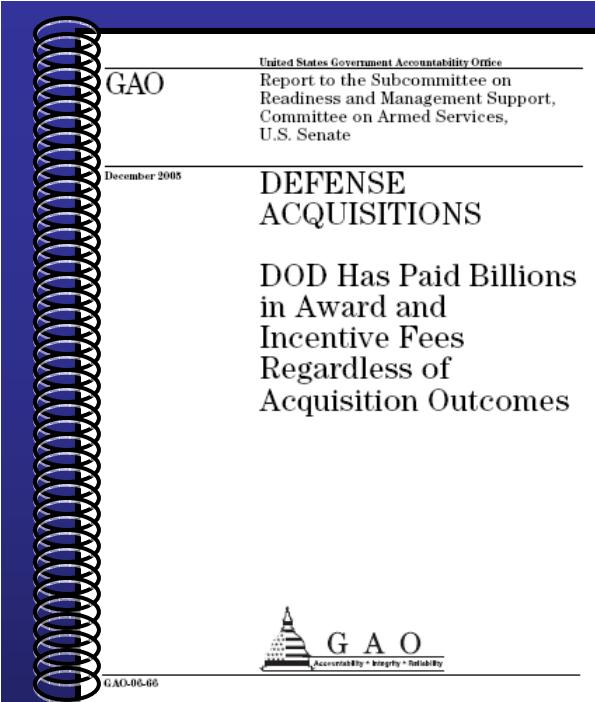
Presented by Rob Tremaine

Associate Dean for Outreach & Performance Support
Defense Acquisition University
West Region
San Diego, CA 92147
619-524-4811
robert.tremaine@dau.mil

Incentive Contracts Research Overview Briefing
Defense Acquisition University (DAU), 17 May 2007

The PROBLEM :

GAO Found Award/Incentive Fee Generally Ineffective



Despite paying billions in fees, DOD has little evidence to support its belief that these fees improve contractor performance and acquisition outcomes. The department has not compiled data, conducted analyses, or developed performance measures to evaluate the effectiveness of award and incentive fees. In addition, when contracts have utilized different fee strategies to focus the contractor's attention on specific acquisition outcomes, contracting officials have stated that DOD has few mechanisms to share lessons learned and innovative practices outside the local level.

What GAO Found

The power of monetary incentives to motivate excellent contractor performance and improve acquisition outcomes is diluted by the way DOD structures and implements incentives. While there were two examples in our sample in which the Missile Defense Agency attempted to link award fees directly to desired acquisition outcomes, such as demonstrating a capability within an established schedule, award fees are generally not linked to acquisition outcomes. As a result, DOD has paid out an estimated \$8 billion in award fees to date on the contracts in our study population, regardless of outcomes. The following selected programs show this disconnect.

Program Performance and Award-Fee Payments on Selected DOD Development Programs				
	Comanche reconnaissance attack helicopter	F/A-22 Raptor tactical fighter aircraft	Joint Strike Fighter tactical fighter aircraft	Space-Based Infrared System High
Acquisition outcomes				
Research and development cost increase over baseline	\$3.7 billion 41.2 percent	\$10.2 billion 47.3 percent	\$10.1 billion 30.1 percent	\$3.7 billion 99.5 percent
Acquisition cycle time increase over baseline	33 months 14.8 percent	27 months 13.3 percent	11 months 5.9 percent	More than 12 months
Percentage and total award fee paid to prime systems contractor (adjusted for rollover) ^a	85 percent \$202.5 million	91 percent \$848.7 million	100 percent \$494.0 million	74 percent \$160.4 million

Sources: DOD submissions to GAO, contract documentation, and GAO-05-301 (data); GAO (analysis).

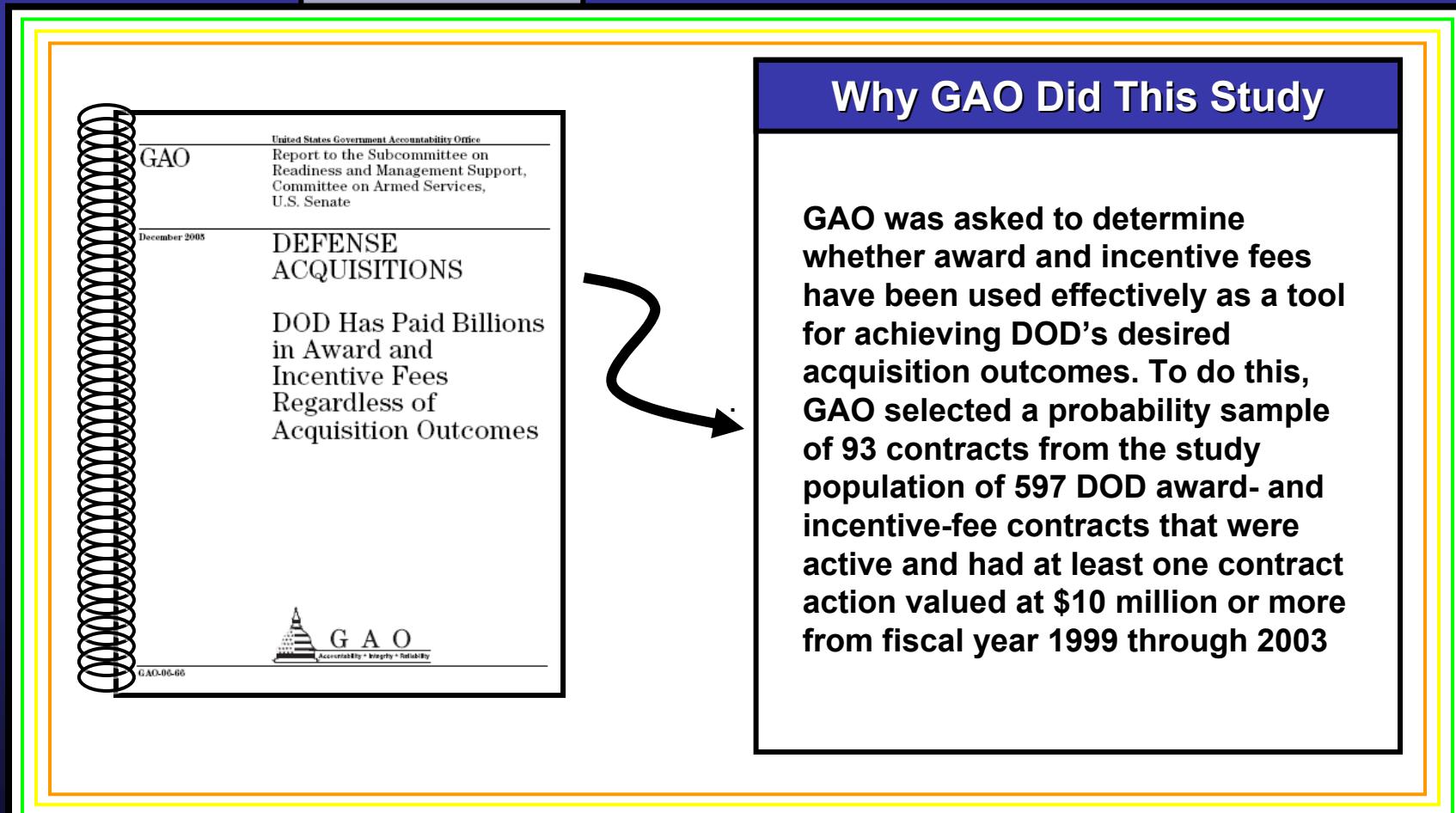
^aWhen calculating the percentage of award fee paid (i.e., percentage of award fee paid = total fee paid to date / (total fee pool – remaining fee pool)), we included rolled-over fees in the remaining fee pool when those fees were still available to be earned in future evaluation periods.

What GAO Recommends

GAO recommends that DOD improve its use of fees by specifically tying them to acquisition outcomes in all new award- and incentive-fee contracts, maximizing contractors' motivation to perform, and collecting data to evaluate the effectiveness of fees. In its comments on a draft of this report, DOD concurred or partially concurred with all of the recommendations.

Award and Incentive Fee Contracts

Background



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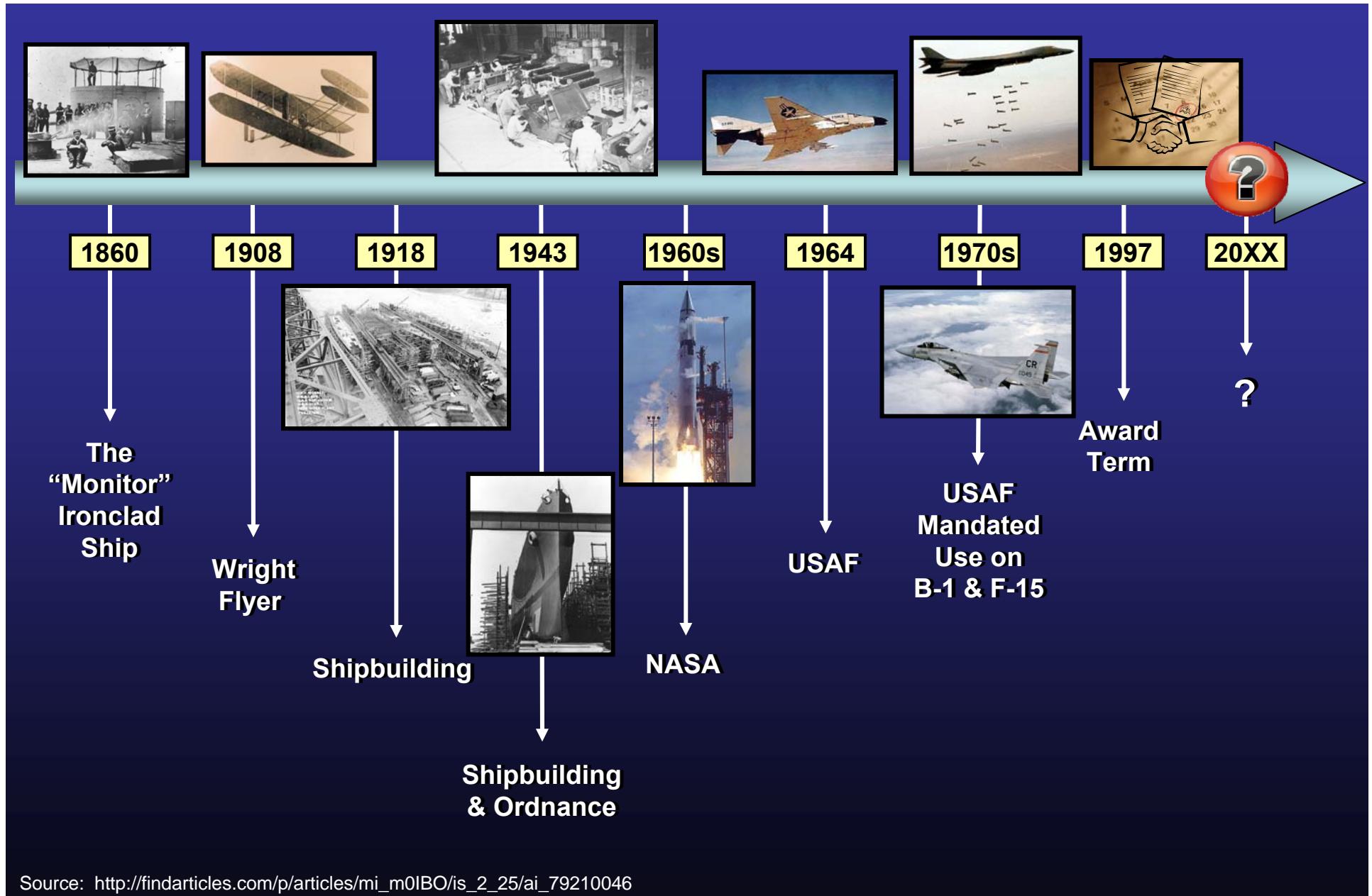
GAO Report Cover:

- United States Government Accountability Office
- Report to the Subcommittee on Readiness and Management Support, Committee on Armed Services, U.S. Senate
- December 2005
- DEFENSE ACQUISITIONS**
- DOD Has Paid Billions in Award and Incentive Fees Regardless of Acquisition Outcomes
- GAO-06-66

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GAO was asked to determine whether award and incentive fees have been used effectively as a tool for achieving DOD's desired acquisition outcomes. To do this, GAO selected a probability sample of 93 contracts from the study population of 597 DOD award- and incentive-fee contracts that were active and had at least one contract action valued at \$10 million or more from fiscal year 1999 through 2003

Incentive Contracts Have Been Used in Various Forms for Some Time



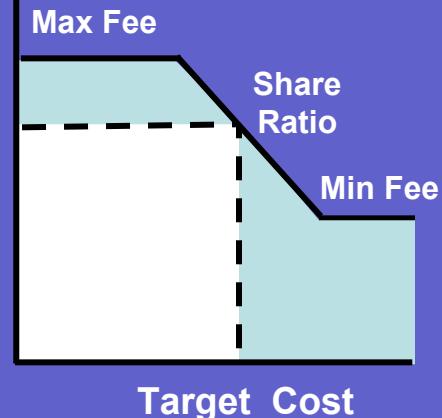
Simplified View of Incentive Contracts

INCENTIVE CONTRACTS

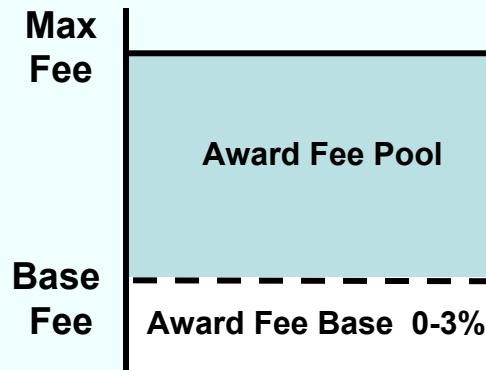
(FAR 16.401)

- Designed to obtain specific acquisition objectives
- Establishes reasonable and attainable targets that are clearly communicated
- Includes appropriate incentive arrangements designed to:
 - Motivate contractor efforts that might not otherwise be emphasized
 - Discourage contractor inefficiency and waste

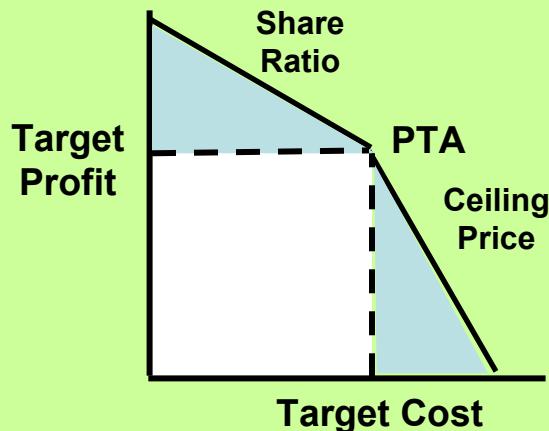
Cost Plus Incentive Fee



Cost Plus Award Fee



Fixed Price Incentive Fee



Incentive Contracts: A Sampling of Recent Assessments and Guidance



Army (ACA) Award Fee Board Member
Guide (September 2003)



Army (ACA) Award Fee Contracts Guide
(September 2003)



Air Force (AFMC) Award Fee & Award
Term Guide, Dec 2002



Army (ACA) Cost & Price Analysis
Handbook, February 2004



Air Force (Secretary of the Air Force) Contract
Incentives Policy 06A-003 - April 04, 2006



Army (U.S. Army Audit Agency) - Best
Practices for Using Award Fees, Audit Report
AA 01-169, February 2001



Air Force Award Fee Guide - March 2002



2001 Incentive Strategies for Defense
Acquisitions Guide



DCAA Contract Audit Manual, March 2006



OUSD Award Fee Contracts (FAR 16, DFARS 215,
DFARS 216) Policy Memo, March 29, 2006



DFARS SUBPART 216.4--INCENTIVE
CONTRACTS (Revised March 21, 2006)



2006 Secretary of the Air Force for Acquisition
Directorate (SAF/AQX) Contract Incentives Study



USAID Guidance for Award
Fee Contracting



Air Force Space Command's Space & Missile
Center (SMC) 2006 Draft Incentives Guide

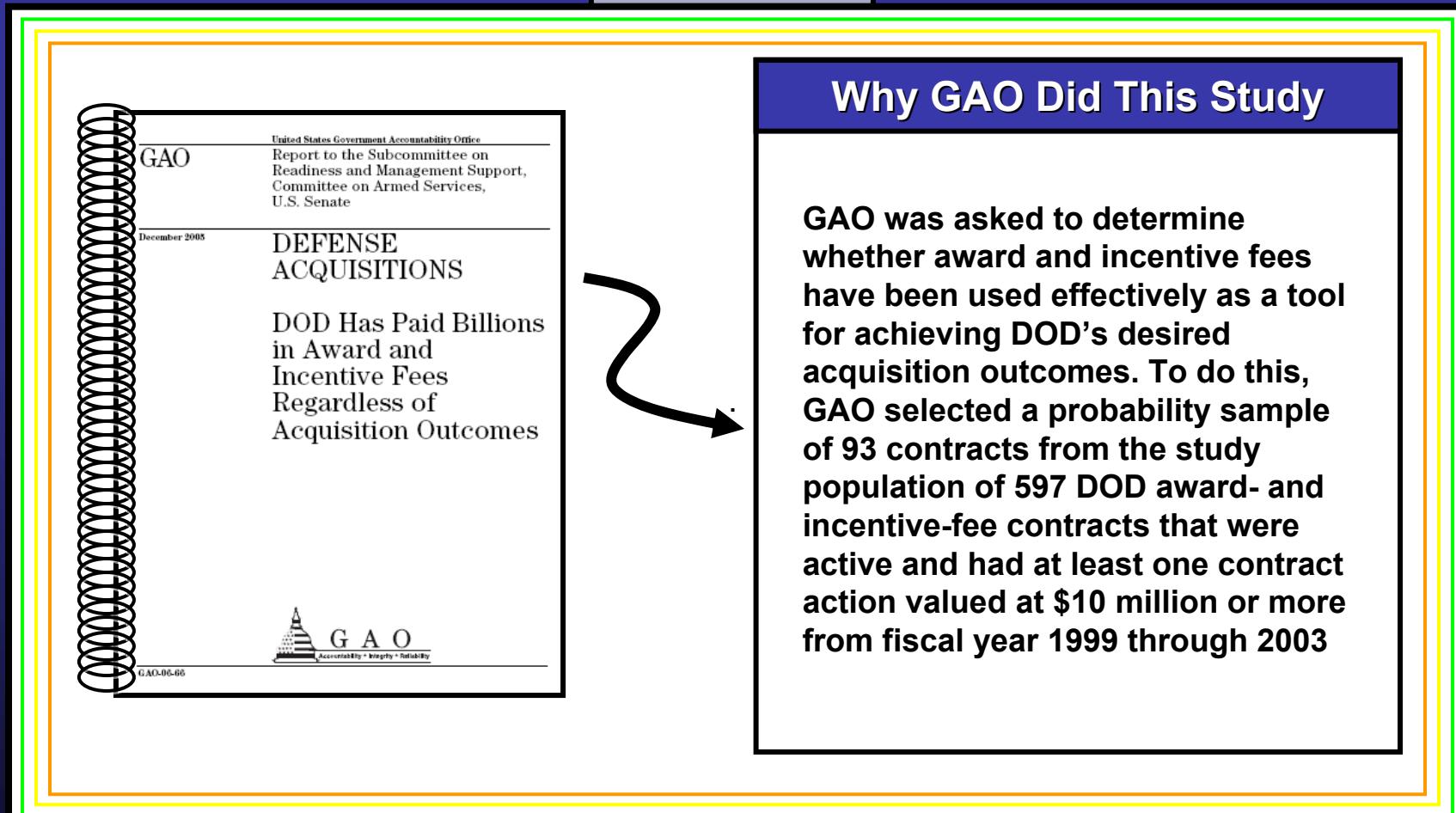


Air Force (SAF/AQC) Award Term/Incentive
Options Guide - January 2003

2007 National Defense Authorization Act, PUBLIC
LAW 109-364—OCT. 17, 2006, SEC. 814

Award and Incentive Fee Contracts

Study Proposal



GAO United States Government Accountability Office
Report to the Subcommittee on Readiness and Management Support, Committee on Armed Services, U.S. Senate

December 2005 DEFENSE ACQUISITIONS

DOD Has Paid Billions in Award and Incentive Fees Regardless of Acquisition Outcomes

GAO G A O Accountability • Integrity • Reliability GAO-06-66

Why GAO Did This Study

GAO was asked to determine whether award and incentive fees have been used effectively as a tool for achieving DOD's desired acquisition outcomes. To do this, GAO selected a probability sample of 93 contracts from the study population of 597 DOD award- and incentive-fee contracts that were active and had at least one contract action valued at \$10 million or more from fiscal year 1999 through 2003

Research Problem Statement & Objective

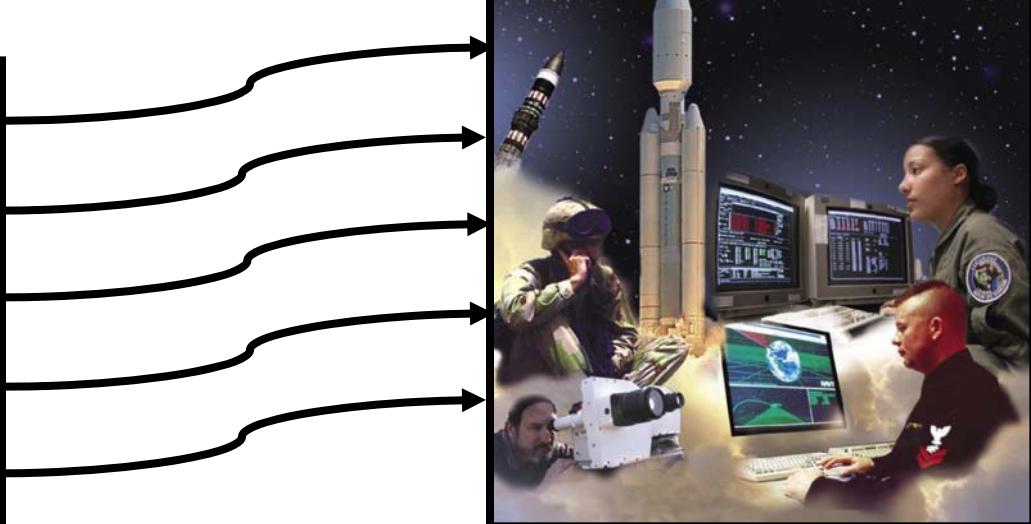
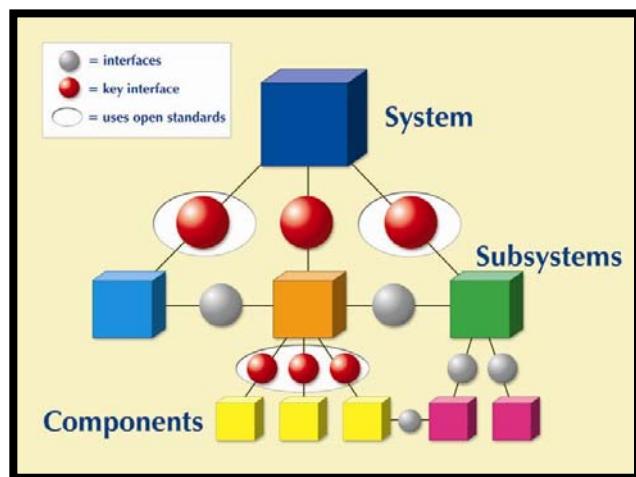
Problem Statement

- The Implementation of Award/Incentive Fee contracts in DoD are not producing the desired/intended outcomes. In some cases, the Acquisition community may not be implementing Award Fee/Incentive contracts, correctly.

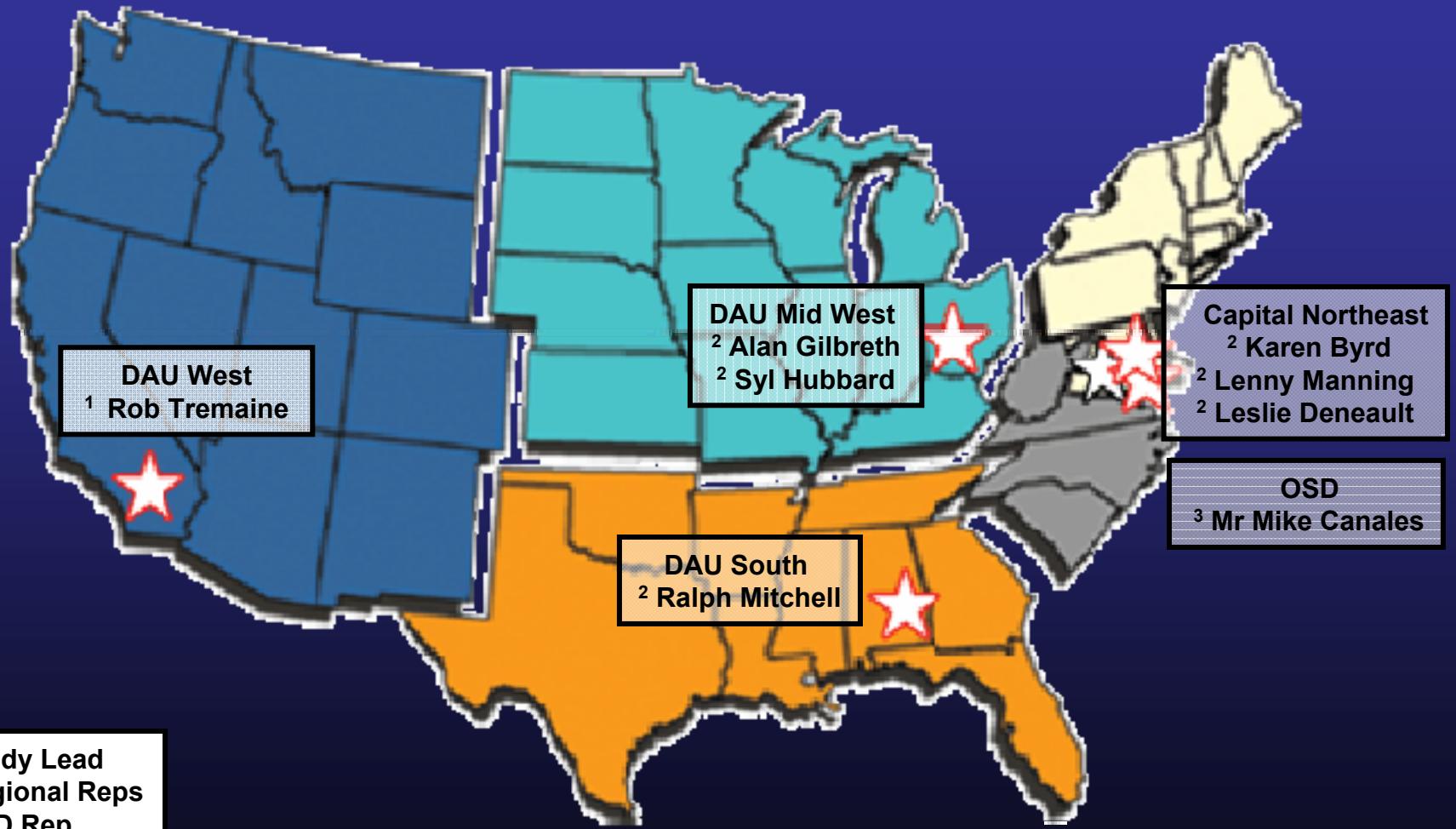
Research Objective

- DAU needs to understand where Award Fee/Incentive Fee made a favorable difference and why.

The Teams' Outcome Will Be A Research Project Rather than a Re-clama to the GAO Findings



Multi-Regional Award/Incentive Fee Study Team



Research Assumptions

Award/Incentive Fee Assumptions:

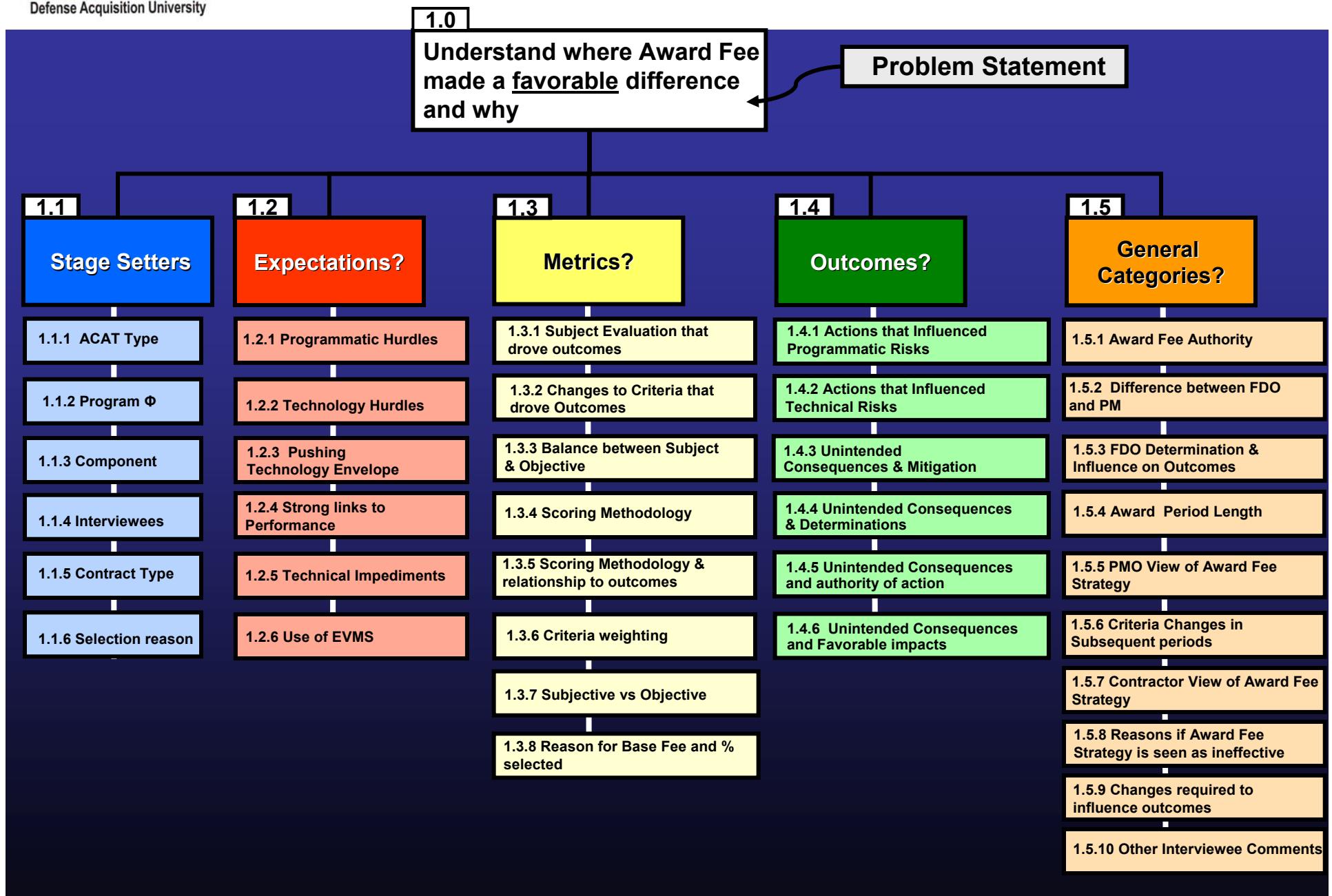
- 1. Improved Contractor Performance Has Not Always Been Achieved Through the Use Of Award Fee/Incentive Fee Contracts.**
- 2. GAO Has Identified Numerous Award/Incentive Fee Contracts that Have Cost the Government Millions Without Always Producing Desired Contractual Outcomes.**
- 3. In DoD Contracting, Award/Incentive Fee Contracts Can Be Powerful Tools to Favorably Influence Contractor Performance in conjunction with good acquisition fundamentals.**
- 4. Empirical Evidence/Measurable Results Should Play a Pivotal Role In Award/Incentive Fee Determinations.**
- 5. GAO Conclusions on the Ineffectiveness Of Award/Incentive Fee Contracting May Be A Result Of Certain Ineffective Practices that Could Be Undermining Policy**

Exchange with the GAO

Met with Mr Tom Denomme and Mr Ron Schwenn on 20 Jun 06 at GAO HQ in DC— *very informative exchange—their comments:*

- Research effort looked for connection between AF/IF and favorable outcomes but they found little evidence to substantiate relationship
- Process seemed to be well understood—no chronic problems
- Found no issues with Policy
- Service Guidelines governing implementation of AF/IF is different—should it be?
- Award Fee sometimes drives requirements creep
- Performance outcomes were sometimes unrealistic--contractor couldn't deliver
- Surprisingly, TPMs didn't seem to play much into the equation
- GAO did not evaluate weighting methodology--would it have made a difference?
- In some cases, AF was seen and used by PM as a “Risk Management” device—is that a bad idea?
- FDO's final evaluation letters don't contain much substantiation—why is it so general?
- The contractor isn't encouraged to pursue alternate COAs especially if they or the government run into [anticipated] programmatic obstacles

Survey Approach Used A WBS Approach



Data Collection Instrument

INCENTIVE FEE and AWARD FEE SURVEY QUESTIONS

SECTION I. PROGRAMMATICS

1. What best describes your program?
 - a. ACAT I
 - b. ACAT IA
 - c. ACAT II
 - d. ACAT III
 - e. Other
2. What best characterizes your program?
 - a. System Development & Demonstration
 - b. Production and Deployment
 - c. Operations & Support
 - d. Other
3. What is your service component?
 - a. Army
 - b. Navy
 - c. Air Force
 - d. Other
4. What is your principle role?
 - a. Program Manager/Director/Project Manager
 - b. Contracting Officer
 - c. Systems Engineer
 - d. Other
5. Did you choose an incentive fee or award fee?
 - a. Incentive Fee
 - b. Award Fee
 - c. Award Fee with Incentives
 - d. Other
6. What were the principal reasons you selected the answer to question 5?
7. If you chose an Incentive Fee, go to Section II
8. If you chose an Award Fee, go to Section III

SECTION II: INCENTIVE FEE (defined as CPIF and FPIF type contracts)

A. EXPECTATIONS

1. What incentives did you use?
2. Why did you choose these incentives?
3. Did the incentives you chose create any unintended consequences?
4. If you faced funding issues, what actions did you take to motivate the contractor to help sustain favorable performance outcomes?

B. METRICS

1. How did you determine the minimum performance level that would motivate the contractor to perform?
2. What metric(s) did you use to incentive the contractor? What was the methodology did you use?
3. How did your methodology lead to success?

C. OUTCOMES

1. Did the contractor stay within the contract performance levels? If so, what were the outcomes in terms of cost and performance?
2. If as a result of the incentives used the contractor did not meet the performance levels, what steps did you take to mitigate those consequences in future contracts?
3. In retrospect, which of the incentives used were most effective in overcoming unintended consequences and leading to favorable performance outcomes?

D. GENERAL CATEGORY

1. How does your organization view your response?
 - a. Very effective in motivating the contractor
 - b. Moderately effective in motivating the contractor
 - c. Somewhat effective in motivating the contractor
 - d. Not very effective in motivating the contractor
2. If you answered "D" above, what is your organization's view of the Incentive Fee as "not very effective"?
 - a. Not everyone is well-trained on Incentive Fees
 - b. Not everyone is aware of the components and developing the incentives
 - c. Other (explain)
3. How does your contractor view your response?
 - a. Very Effective
 - b. Moderately effective
 - c. Not very effective
4. In retrospect, what changes, if any, would you make to the Award Fee Plan to influence performance outcomes even more?
 - a. None—it worked just fine
 - b. More vigorously apply ...
5. What other comments do you have concerning the Incentive Fee?

SECTION III. AWARD FEE (Defined as CPAF and FPAF type contracts)

A. EXPECTATIONS

1. What were your primary programmatic hurdles?
2. What were your primary technology hurdles?
3. Where are you pushing the technology envelope?
4. What were your award fee objectives that created a balance between cost and performance?
5. How did you establish the criteria used in the award fee determination?
6. What programmatic and/or technical impediments were identified and resolved/reconciled during the Award Fee periods?
7. Did you and, if so, how did you use EVMS to influence the award fee determination?
8. If you faced funding issues, what Award Fee actions did you take to motivate the contractor to help sustain favorable performance outcomes?

B. METRICS

1. What were your subjective evaluation criteria that influenced the award fee determination?
2. What changes did you make to the award fee criteria that drove favorable outcomes and why?
3. How did you determine the balance/share between cost and performance and what had the most favorable impact on performance?
4. What was your scoring methodology?
5. How did your scoring methodology (and rating definitions) influence the award fee determination?
6. What criteria did you weigh more heavily than others and why?
7. What did you weigh evenly and why did this weight influence the award fee determination?
8. Could you have replaced any of the subjective criteria with objective criteria that would have favorable impacts on performance outcomes?
9. If you used a Base Fee, why did you use it and what was the balance between cost and performance?

C. OUTCOMES

1. What specific Award Fee actions did you take that influenced the award fee determination?
 - a. Programmatic risks?
 - b. Technical risks?
2. In retrospect, what worked consistently in the Award Fee determination to influence performance outcomes?
- 3a. If your expected performance outcomes led to unintended consequences, how did you mitigate those unintended consequences?
- 3b. Did those unintended consequences have an impact on the contractor?
- 3c. Did you have the authority to change or eliminate a result of unintended consequences?
- 3d. In retrospect, what methods did you find that worked to overcome unintended consequences and still promote favorable performance outcomes?

D. GENERAL CATEGORY

1. Who made the final Award Fee determination?

Under Configuration Control: 2006 0702 Version 6

2. If the Award Fee Determination Official (FFO) was different from the Program Manager/Program Director, was the Award Fee decision different than what the PM recommended? If so, why?
3. How did the FDO determination favorably influence the expected outcome?
4. If earlier Award Fee decisions realized less tangible outcomes, what subjective or objective criteria/weighting were changed in subsequent award fee periods to influence favorable performance outcomes and why?
5. What is the length of time between your award fee periods? Why did you select that period of time? Were they too short or too long?
6. How does your organization view your Award Fee strategy? **Please elaborate after your response.**
 - a. Very effective in motivating the contractor
 - b. Moderately effective in motivating the contractor
 - c. Somewhat effective in motivating the contractor
 - d. Not very effective in motivating the contractor
7. If you answered "D" above, what is the principle reason your organization might view the Award Fee as "not very effective"? **Please elaborate after your response.**
 - a. Not everyone is well-trained on Award Fee
 - b. Not everyone is aware of the complicating factors that are considered in the decision equation
 - c. Other
8. How does your contractor view your Award Fee strategy?
9. In retrospect, what changes, if any, would you make to the Award Fee Plan to influence performance outcomes even more?
10. What has been your Contractor response to your determinations?
11. What other comments do you have concerning Award Fee?

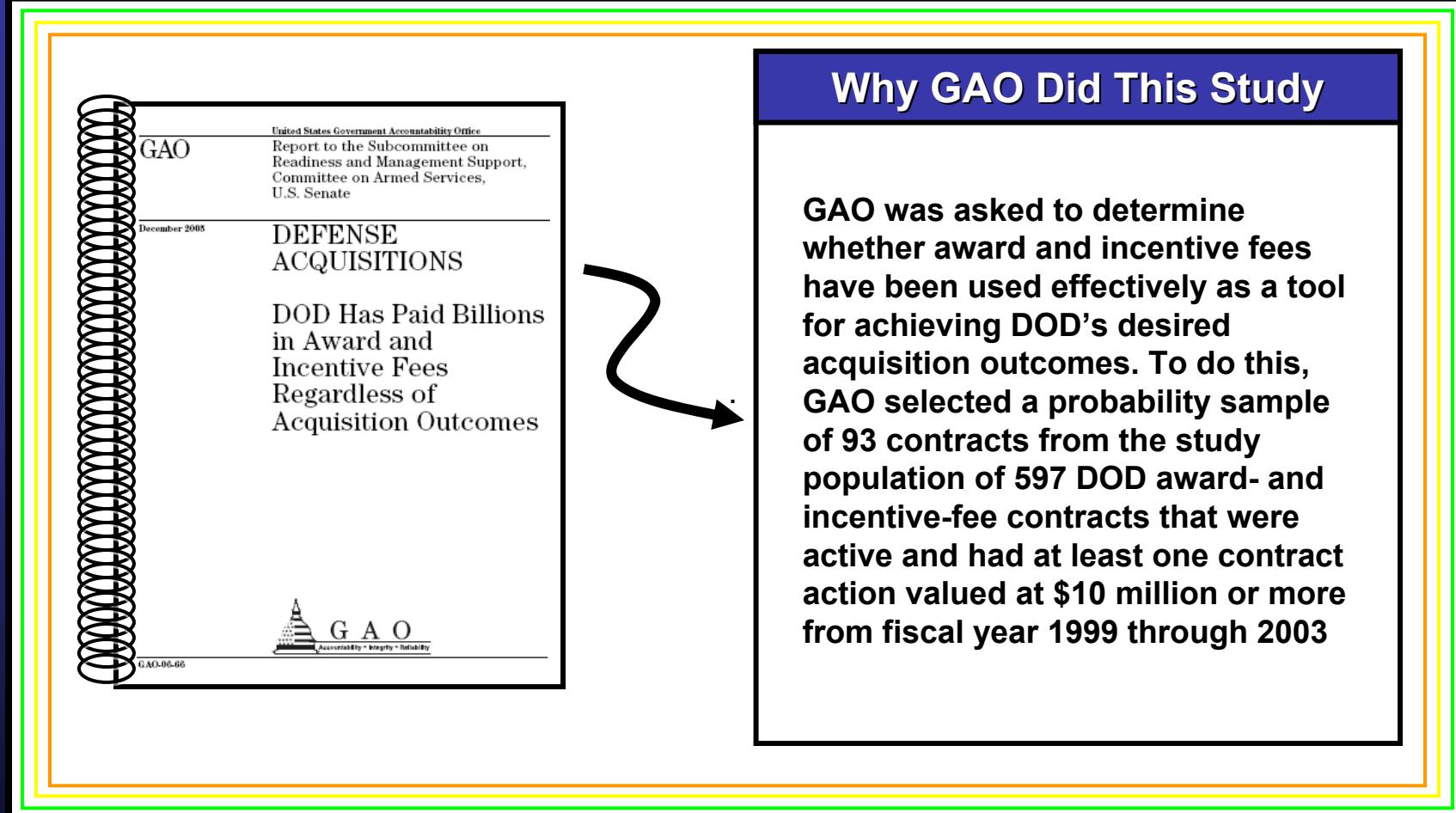
Incentive Contract Study Interviews By Region



West Region	Mid-West	South	CNE/MA
+	SBIRS High	+	B-2
+	GPS	+	C-17
+	RAIDRS	+	F-15
+	AEHF	+	F-16
+	STSS	+	Global Hawk
+	AFSCN	+	Global Transportation Network
		+	AMC Contractor Tactical Terminal Operations
		+	FCS
		+	Total Integrated Engine Revitalization
		+	Biological Detection System
+ Completed Interviews			

Award and Incentive Fee Contracts

Study Findings



GAO United States Government Accountability Office
Report to the Subcommittee on Readiness and Management Support, Committee on Armed Services, U.S. Senate

December 2005 DEFENSE ACQUISITIONS

DOD Has Paid Billions in Award and Incentive Fees Regardless of Acquisition Outcomes

GAO G A O Accountability • Integrity • Reliability GAO-06-66

Why GAO Did This Study

GAO was asked to determine whether award and incentive fees have been used effectively as a tool for achieving DOD's desired acquisition outcomes. To do this, GAO selected a probability sample of 93 contracts from the study population of 597 DOD award- and incentive-fee contracts that were active and had at least one contract action valued at \$10 million or more from fiscal year 1999 through 2003

... and the Findings Say:



1. Strongly Communicate Expectations and Continually Provide Feedback

Stage Setters	Expectations?	Metrics?	Outcomes?	General Categories?
1.1.1 ACAT Type	1.2.1 Programmatic Hurdles	1.3.1 Subject evaluation that drove outcomes	1.4.1 Actions that Influenced Programmatic Risks	1.5.1 Award Fee Authority
1.1.2 Program Type	1.2.2 Technology Hurdles	1.3.2 Changes to Criteria that drove Outcomes	1.4.2 Actions that Influenced Technical Risks	1.5.2 Emphasis between PDO and PM
1.1.3 Component	1.2.3 Technology Envelope	1.3.3 Relationship between Subject & Objective	1.4.3 Unintended Consequences & Mitigation	1.5.3 PDO Determinants of Influence on Outcomes
1.1.4 Interviewee	1.2.4 Strong Links to Requirements	1.3.4 Scoring Methodology	1.4.4 Unintended Consequences & Determinants	1.5.4 Award Period Length
1.1.5 Contract Type	1.2.5 Technical Impediments	1.3.5 Scoring Methodology & relationship to outcomes	1.4.5 Unintended Consequences and authority of action	1.5.5 PMO View of Award Fee Strategy
1.1.6 Selection reason	1.2.6 Use of EVMG	1.3.6 Criteria weighting	1.4.6 Unintended Consequences and Favorable Impacts	1.5.6 Criteria Changes in Subsequent periods
		1.3.7 Subjective vs Objective		1.5.7 Contractor View of Award Fee Strategy
		selected		1.5.8 PDO View of Award Fee Strategy as Ineffective
				1.5.9 Changes required to influence outcomes
				1.5.10 Other Interviewee Comments

... and the Findings Say:



2. Use Relevant, Achievable and Enduring Measures Within an Evaluation Period

Stage Setters	Expectations?	Metrics?	Outcomes?	General Categories?
• “Hard-wire” measures to achievable outcomes				
• Employ technical performance goals and cost controls	1.3.1 Subject Evaluation that	1.4.1 Actions that Influenced	1.5.1 Award Fee Authority	
• Jointly develop incentive criteria with contractors since they tend to be more strongly correlated to outcomes	1.3.2 Changes to Criteria that	1.4.2 Actions that Influenced	1.5.2 Difference between FDO	
• Select Key outcomes that make evaluation periods more enduring by creating a bridge between one award fee period and the next	1.3.3 Balance between Subject	1.4.3 Unintended Consequences	1.5.3 FDO Determination & Influence on Outcomes	
• Use subjective measures to drive critical processes, management responsiveness, and certain behavior	1.3.4 Strong Links to	1.4.4 Unintended Consequences	1.5.4 Award Period Length	
• Institute a combined objective and subjective measures strategy	1.3.5 Scoring Methodology	1.4.5 Unintended Consequences	1.5.5 DMO View of Award Fee	
	1.3.6 Criteria weighting	1.4.6 Unintended Consequences and Favourable Impacts	1.5.6 Criteria Changes in Subsequent periods	
	selected			
			1.5.7 Reasons if Award Fee Strategy is seen as Ineffective	
			1.5.8 Changes required to	
			1.5.9 Other Interviewee Comments	

... and the Findings Say:



3. Use Base Fee in Award Fee Contracts

1.1	1.2	1.3	1.4	1.5
Stage Setters	Expectations?	Metrics?	Outcomes?	General Categories?
1.1.1 ACAT Type efforts	1.2.1 Programmatic Hurdles	1.3.1 Subject Evaluation that drove outcomes	1.4.1 Actions that Influenced Programmatic Risks	1.5.1 Award Fee Authority
1.1.2 Program Ø	1.2.2 Technology Hurdles	1.3.2 Changes to Criteria that drove Outcomes	1.4.2 Actions that Influenced Technical Risks	1.5.2 Difference between FDO and PM
1.1.3 Component	1.2.3 Pushing Technology Envelope	1.3.3 Balance Between Subject & Objective	1.4.3 Unintended Consequences & Mitigation	1.5.3 Determination & Influence on Outcomes
1.1.4 Interviewees	1.2.4 Strong links to Performance	1.3.4 Scoring Methodology	1.4.4 Unintended Consequences & Determinations	1.5.4 Award Period Length
1.1.5 Contract Type	1.2.5 Unintended Consequences	1.3.5 Subjective vs Objective relationship to outcomes	1.4.5 Unintended Consequences and authority of action	1.5.5 PMO View of Award Fee Strategy
1.1.6 Selection reason	1.2.6 Use of EVMA	1.3.6 Criteria Weighting	1.4.6 Unintended Consequences and Favorable Impacts	1.5.6 PMO View of Award Fee Strategy
		1.3.7 Subjective vs Objective		1.5.7 PMO View of Award Fee Strategy
		Reason for Base Fee and % selected		1.5.8 Reasons if Award Fee Strategy is seen as Ineffective
				1.5.9 Changes required to influence outcomes
				1.5.10 Other Interviewee Comments

... and the Findings Say:



4. Institute Training and Leverage Experienced Personnel to the Maximum Extent

Stage Setters

Expectations?

Metrics?

Outcomes?

1.51

General Categories?

- Incorporate the practical experience of many already embedded talented personnel
- Establish formalized instruction and continue to coach personnel on use of incentives
- Require performance monitors to observe other assessments to help them appreciate the depth of evaluations
- Encourage “Specialty” training for key personnel who administer incentive contracts

1.1.1 ACAT Type

1.2.1 Programmatic Hurdles

1.3.1 Subject Evaluation that

1.4.1 Actions that Influenced

1.5.1 Award Fee Authority

1.1.2 Program o

1.2.2 Technology Hurdles

1.3.2 Changes to Criteria that

1.4.2 Actions that Influenced

1.5.2 Difference between FDO

1.1.3 Component

1.2.3 Pushing

1.3.3 Balance between Subject

1.4.3 Unintended

1.5.3 FDO Determination &

1.1.4 Interviewees

1.2.4 Strong links to

1.3.4 Scoring Methodology

1.4.4 Unintended

1.5.4 Award Period Length

1.1.5 Contract Type

1.2.5 Technical Impediments

1.3.5 Criteria relationship to outcomes

1.4.5 Unintended

1.5.5 View of Award Fee

1.1.6 Selection reason

1.2.6 Use of EVMS

1.3.6 Criteria weighting

1.4.6 Unintended

1.5.6 Criteria Changes in

evaluations

1.3.7 Subjective vs Objective

1.4.7 Unintended

1.5.7 Contractor View of Award Fee

and authority of action

1.4.8 Unintended

1.5.8 View of Award Fee

Consequences and Favorable Impacts

1.4.9 Unintended

1.5.9 Changes required to

selected

1.4.10 Unintended

1.5.10 Other Interviewee Comments

and authority of action

1.4.11 Unintended

1.5.11 Contractor View of Award Fee

Consequences and Favorable Impacts

1.4.12 Unintended

1.5.12 Contractor View of Award Fee

and authority of action

1.4.13 Unintended

1.5.13 Contractor View of Award Fee

Consequences and Favorable Impacts

1.4.14 Unintended

1.5.14 Contractor View of Award Fee

and authority of action

1.4.15 Unintended

1.5.15 Contractor View of Award Fee

Consequences and Favorable Impacts

1.4.16 Unintended

1.5.16 Contractor View of Award Fee

and authority of action

1.4.17 Unintended

1.5.17 Contractor View of Award Fee

Consequences and Favorable Impacts

1.4.18 Unintended

1.5.18 Contractor View of Award Fee

and authority of action

1.4.19 Unintended

1.5.19 Contractor View of Award Fee

Consequences and Favorable Impacts

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and authority of action

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Consequences and Favorable Impacts

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Consequences and Favorable Impacts

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and authority of action

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Consequences and Favorable Impacts

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1.5.26 Contractor View of Award Fee

and authority of action

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1.5.27 Contractor View of Award Fee

Consequences and Favorable Impacts

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and authority of action

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Consequences and Favorable Impacts

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Consequences and Favorable Impacts

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Consequences and Favorable Impacts

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Consequences and Favorable Impacts

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and authority of action

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Consequences and Favorable Impacts

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Consequences and Favorable Impacts

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Consequences and Favorable Impacts

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and authority of action

1.4.79 Unintended

1.5.79 Contractor View of Award Fee

Consequences and Favorable Impacts

1.4.80 Unintended

1.5.80 Contractor View of Award Fee



5. Carefully Weigh Industry Concerns

“Government Construction of the Award Fee Plan (Including Metrics, Incentives, etc.)

May Not Link With the Offeror’s Proposed Solution Or Motivations

- Award Fee Sometimes isn’t Proper Contract Type to Achieve Program Outcomes
- In Some Cases, the Intended Goal(s) of Award Fee Contracts are Unclear
- Contracts Without Base Fee Can Cause Problems
- In Some Cases, the Government Does Not Follow Its Own Policies On Award Fee
- On Occasion, Award Fee Evaluation Criteria Are Poorly Explained Or Justified and Communication of Award Fee Goals and Criteria Are Not Clearly Explained
- It Is Difficult to Establish the Relationship Between Awards For month-to-month Activities to the Goals Of A Multiple-Year Program. The Linkage Is Not Always Apparent
- Administration of Award Fee Criteria Can Change Post Award and Create Problems During Contract Execution
- Government May Not Manage Or Evaluate Award Fee Criteria as Agreed /Planned
- Post-award administration of Award Fee contracts is time and resource intensive

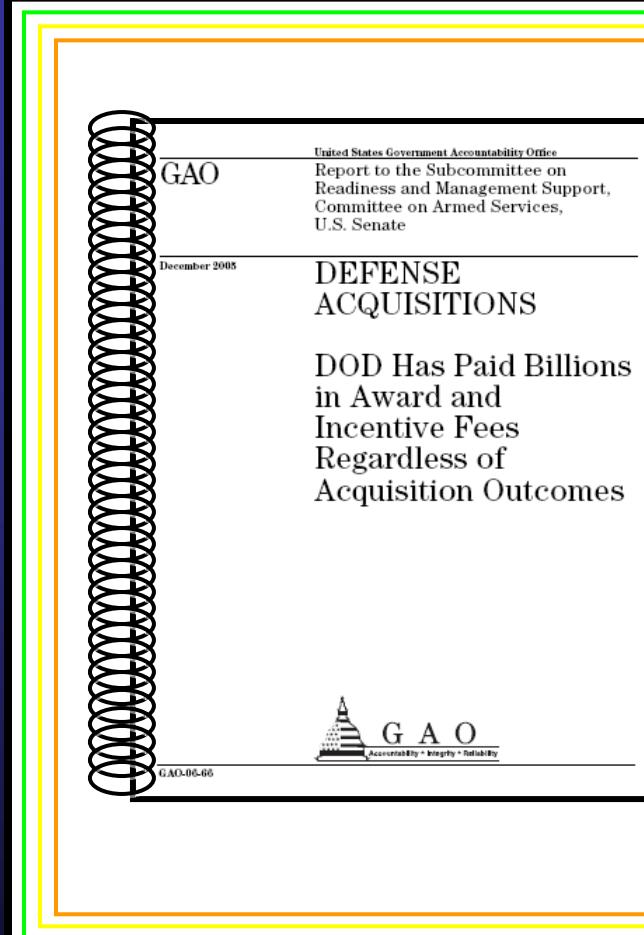


5. Carefully Weigh Industry Concerns

- Government Personnel Are Not Adequately Trained in Managing Award Fee Contracts
- Desired Outcomes Are Not Always Driven By The Award Fee Because Of Insufficient Funds Available and Subjectivity Of The Final Evaluation.
- Inconsistency In the Timing Of the Award In Line With The Evaluation Criteria And Uncertainly Of Expected Profitability Before Award Pose Additional Problems
- Contracting Parties /Stakeholders have Different Perceptions of Award Fees Purposes
- In Some Cases, There Is Government Failure to Understand the Economics of Defense Contracting and Its Impact On Government Contractors
- From Time to Time, There is Inappropriate Use Of Award Fee Contracts
- Award fee is not targeted at creating fair shareholder value (or financial advantage to the private company) in line with actual performance. Metrics are sometimes not meaningful and are "fuzzy" in line with "fuzzy" requirements. Sometimes they are too subjective and do not measure outcomes that are sought by DoD
- Award fees that require the contractor to exceed the requirements of the contract motivate requirements creep or "goldplating"

Award and Incentive Fee Contracts

Recommendations



The image shows the front cover of a GAO report and a summary slide. The report cover is titled 'GAO' and 'United States Government Accountability Office' with the subtitle 'Report to the Subcommittee on Readiness and Management Support, Committee on Armed Services, U.S. Senate'. It is dated 'December 2005' and has the title 'DEFENSE ACQUISITIONS' with the subtitle 'DOD Has Paid Billions in Award and Incentive Fees Regardless of Acquisition Outcomes'. The GAO logo is at the bottom. A green, orange, and yellow border surrounds the report cover. A black curly arrow points from the report cover to a summary slide on the right. The summary slide has a blue header 'Why GAO Did This Study' and a large block of text explaining the study's purpose and methodology.

Why GAO Did This Study

GAO was asked to determine whether award and incentive fees have been used effectively as a tool for achieving DOD's desired acquisition outcomes. To do this, GAO selected a probability sample of 93 contracts from the study population of 597 DOD award- and incentive-fee contracts that were active and had at least one contract action valued at \$10 million or more from fiscal year 1999 through 2003.

Recommendations

- Maximize two existing Continuous Learning Modules (CLMs) to help guide organizations with their incentive selection and subsequent pathway.
 - Contractual Incentives (CLC-018): focuses on balance between government and industry goals and objectives in crafting an effective incentive strategy
 - Provisional Award Fees (CLC-034): addresses the new 2003 rule that permits award fee payments to be made anytime prior to the interim or final evaluation.
- Exploit the increasingly popular collaborative medium called Communities of Practices (COPs)—DAU has already established a site on the ACC, “Award and Incentive Fee Contracts.” (<https://acc.dau.mil/CommunityBrowser.aspx?id=105550>).
 - Provides access to a wide array of documented lessons learned regarding incentives
 - Provides the community a bridge to the source of experts who face incentive challenges every day
 - Reinforces useful incentive practices and techniques
- Develop a much more comprehensive Incentive Contracts CLM

David M. Walker Comptroller General of the United States

December 21, 2006 Responses to the Subcommittee on Defense, Committee on Appropriations, House of Representatives

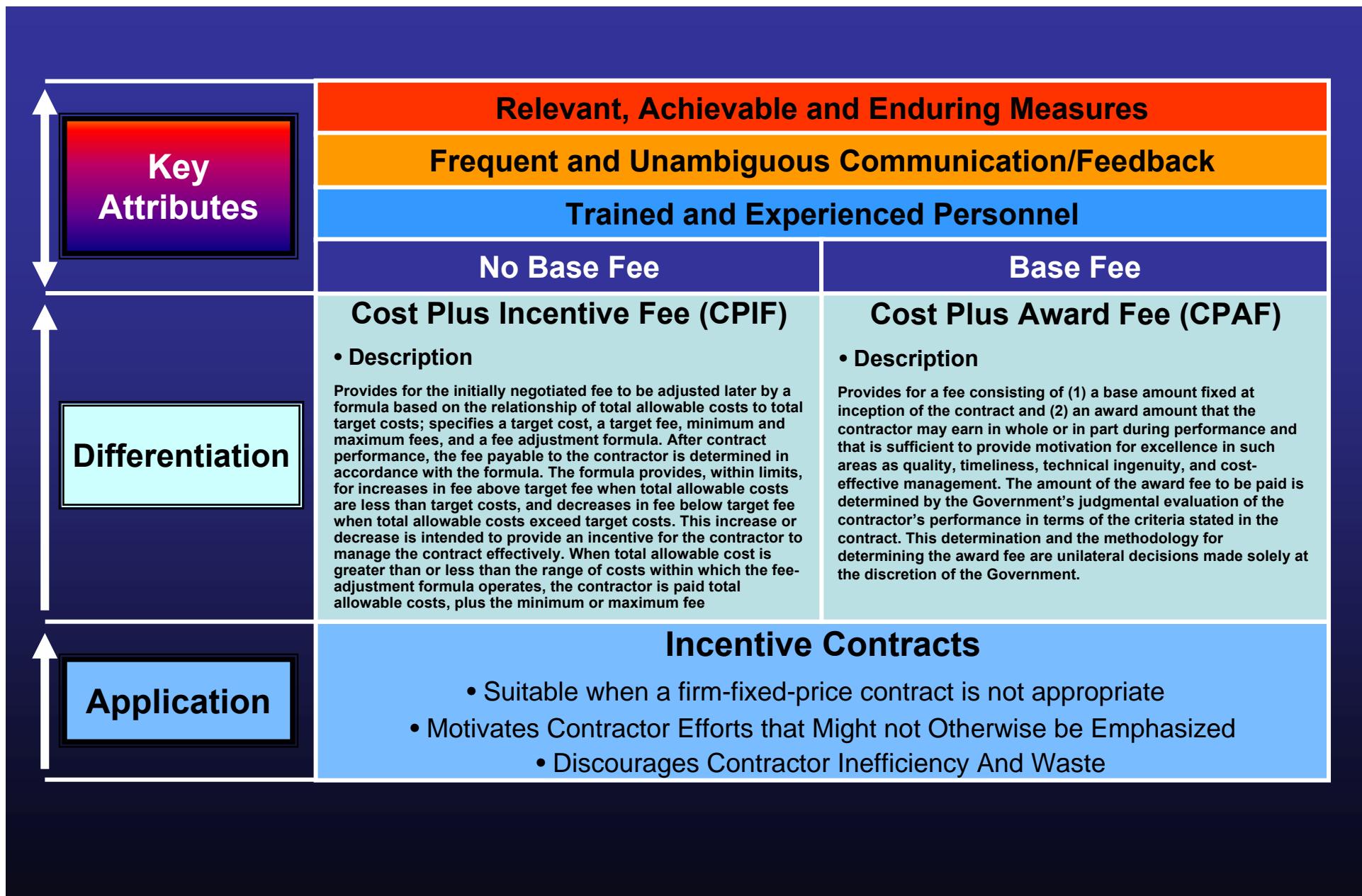
2. Do you believe they are an effective way to create incentives with contractors? In other words, do they improve contractor performance?

Award and incentive fees can be an effective tool if properly designed and effectively administered. However, for these fees to be effective, DOD must address the underlying problems in its acquisition system and more directly link the fees to the outcomes it wants. Because the weapon system programs that result from this system are in many cases unexecutable and/or subject to changing "requirements" or funding levels, DOD has been unwilling to hold its programs or its contractors accountable for achieving the very acquisition outcomes it has identified. As a result, fees are paid even when outcomes do not meet expectations. Addressing these broader acquisition issues and strengthening the link between fees and acquisition outcomes can increase the accountability of DOD programs for fees paid, of contractors for results achieved, and the likelihood that these fees will motivate the contractors and be an effective tool for the government.

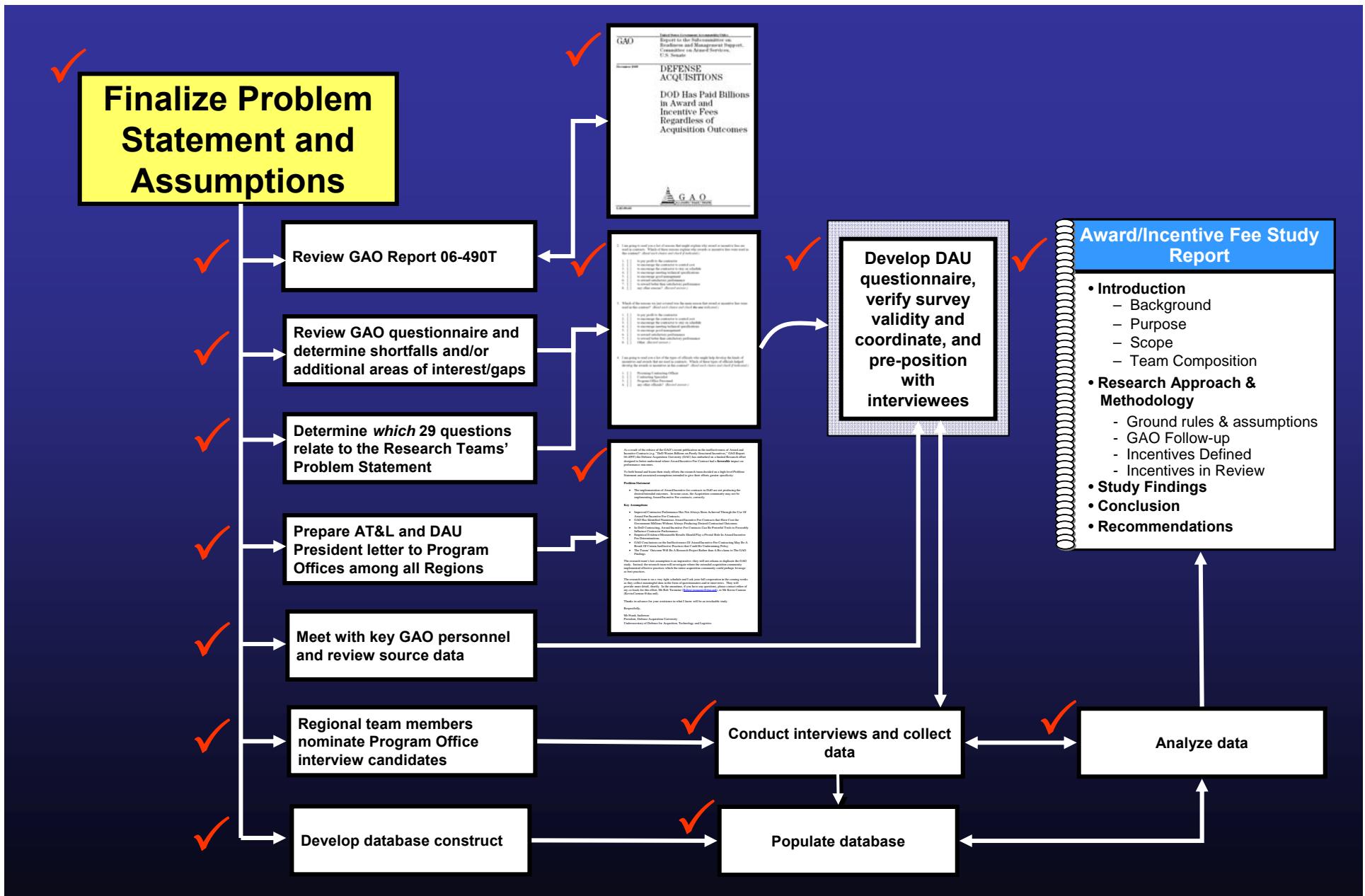
3. Do you believe we should discontinue the use of award and incentive fees?

No, we do not believe they should be discontinued. Award and incentive fees can be useful if they are used in the appropriate setting. Each contract type has a use based on the level of risk involved. The problem occurs when you proceed into programs without realistic requirements and sufficiently mature technologies on which to base realistic cost and schedule estimates and attempt to offset that increased risk by offering award fees to motivate the contractor to overcome that risk. The important question is: Have you adequately defined and established appropriate criteria that enable you to measure outcomes? And finally, how do you apply those criteria in determining the level of fee that can be justified? We have made several recommendations to this effect, and DOD has responded favorably with new guidance to link award fees to acquisition outcomes. However, as with other recommendations we have made related to DOD weapon system acquisitions, the key will be how this new policy is implemented.

An Aggregate View



How this Research Study Came Together





Back-Ups

Management Deliberation Center

- State-of-the-art facility designed and developed to support group collaboration.
- Participants can contribute anonymously and simultaneously, or at different times. The software also collects and tabulates votes, graphically and statistically displays results, and accesses other packages and documents.

